No. 77-1820

In the Supreme Court of the United States

OCTOBER TERM, 1978

INTERSTATE NATURAL GAS ASSOCIATION OF AMERICA AND TEXAS EASTERN TRANSMISSION CORPORATION,
PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

WADE H. MCCREE, JR.,
Solicitor General,
Department of Justice,
Washington, D.C. 20530.

ROBERT R. NORDHAUS,
General Counsel,
Federal Energy Regulatory Commission,
Washington, D.C. 20426.

In the Supreme Court of the United States

OCTOBER TERM, 1978

No. 77-1820

INTERSTATE NATURAL GAS ASSOCIATION OF AMERICA AND TEXAS EASTERN TRANSMISSION CORPORATION, PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioners contend that an accounting rule promulgated by the Commission under Section 8(a) of the Natural Gas Act, 52 Stat. 825, 15 U.S.C. 717g(a), and Section 301(a) of the Federal Power Act, as added, 49 Stat. 854, 16 U.S.C. 825(a),[1] is arbitrary and capricious.

---

[1]Section 8(a) and Section 301(a) provide in pertinent part and in the same terms:

> The Commission may prescribe a system of accounts to be kept by licensees and public utilities [natural-gas companies] and may classify such licensees and public utilities [natural-gas companies] and prescribe a system of accounts for each class. The Commission, after notice and opportunity for hearing, may determine by order the accounts in which particular outlays or receipts shall be entered, charged, or credited. • • •

1. In 1970 in *Manufacturers Light and Heat Company*, 44 F.P.C. 314, the Commission held that for ratemaking purposes, companies subject to its jurisdiction should not treat the gain resulting from their reacquisition of their own debt securities as income in the year of reacquisition, but should amortize the gain over the remaining life of the reacquired debt. Thus, for example, if Company A issued $1 million of debt securities in 1965, to mature in 1975, and was able to repurchase that debt at a discount in 1970 for $750,000, then for ratemaking purposes, the $250,000 gain should not be deemed income in 1970; rather the gain should be spread evenly over the next five years. Although the Commission's rule was a departure from accounting rules generally employed by non-regulated companies, the Commission justified it on the principle that the basic objective of the ratemaking process is to match costs and revenues (see Pet. App. 113). Petitioners do not dispute the propriety of that rule in the ratemaking context.

In 1974, after an informal rulemaking proceeding, the Commission established a rule that companies subject to its jurisdiction must follow the same amortization rule in all their financial statements, which are issued to stockholders and the public generally (Pet. App. 1-96). Petitioners sought review, contending that there was no regulatory need for such uniformity, and that it would adversely affect their ability to issue debt securities. The court of appeals remanded to the Commission for a further explanation of its regulatory need (Pet. App. 97-108). On remand, the Commission issued another opinion adhering to and further explaining its rule (Pet. App. 109-118). The Commission stated, *inter alia* (Pet. App. 111, 115-117):

> Use of a uniform system facilitates comparability which not only aids analysis in rate proceedings, but also assists the Commission in making accurate cost

> of service determinations and helps to assure that jurisdictional utilities will state plant, income, expense and various other accounts in a similar manner.
>
> * * * * *
>
> * * * While the rate policy under *Manufacturers* could be followed regardless of the accounting, consistency between the accounting and ratemaking not only facilitates the ratemaking process, but more importantly, is necessary to avoid financial reporting that obscures the economic realities of the ratemaking process to the detriment of investors and others relying on the financial statements.
>
> * * * * *
>
> * * * We should not impose on the reader of published financial statements the burden of seeking out information in the Commission's individual rate docket files to finally discover that gains (losses) used in calculating reported current net income available to stockholders do not really belong to the stockholders, but instead are to be passed on to consumers in future years through the ratemaking process.

On further review, the court of appeals affirmed (Pet. App. 121-122).

2. Petitioners continue to contend (Pet. 7-12) that the uniformity required by the Commission's rule serves no regulatory need and adversely affects their ability to issue debt securities. The Commission, however, explained that in its judgment uniformity will "assis[t] the Commission in making accurate cost of service determinations" and will prevent confusion among "investors and others relying on the financial statements." Petitioners appear to

dispute that uniformity will have those effects (Pet. 10-12), but that is a judgment for the Commission and it is clearly not arbitrary and capricious.

Moreover, as the Commission noted (Pet. App. 118), there is a certain inconsistency in petitioner's contentions. On the one hand they argue that uniformity exalts form over substance and that full and accurate disclosure can be made in financial statements without such uniformity (Pet. 10-12), while on the other hand they argue that the rule will so affect the appearance of their financial statements as to impair significantly their ability to sell debt financing (Pet. 7-8). Furthermore, notwithstanding petitioners' claim (Pet. 9), petitioners have not shown that the rule has in fact produced the feared result (Pet. App. 118).[2]

Under Section 8(a) of the Natural Gas Act and Section 301(a) of the Federal Power Act, the Commission has express authority to "prescribe a system of accounts" for regulated companies and to "determine by order the accounts in which particular outlays or receipts shall be entered, charged, or credited * * *." Since accounting rules are largely a matter of convention, the discretion to establish particular rules, though not unlimited, is necessarily broad and should not be overturned in the

[2]Indeed, as the Commission also noted (Pet. App. 9), the challenged rule does not prevent petitioners from reflecting the gains from reacquisition of debt; it merely requires that those gains be amortized over a number of years rather than reflected entirely in the year of reacquisition. Assuming *arguendo* that the consequence will be to reduce reported income in a given year and to adversely affect petitioners' ability to sell debt financing in that year, the income would be reported in future years and thus presumably would enhance petitioners' ability to sell debt in those years from what it would have been under petitioners' desired rule. Over a number of years it is difficult to see what difference the rule would make to petitioners' ability to sell debt securities.

absence of a clear abuse of discretion. See, *e.g.*, *United States* v. *New York Telephone Co.*, 326 U.S. 638, 655. No such abuse has been shown here.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

WADE H. MCCREE, JR.,
Solicitor General.

ROBERT R. NORDHAUS,
General Counsel,
Federal Energy Regulatory Commission,

SEPTEMBER 1978.

DOJ-1978-08